UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND

ARNOLD WEINBERG, Derivatively on Behalf of BIOMED REALTY TRUST, INC., Plaintiff,	)	
v.	)	Case 1:11-cv-03116-JKB
ALAN D. GOLD, GARY A. KREITZER, MATTHEW G. MCDEVITT, R. KENT GRIFFIN, JR., BARBARA R. CAMBON, EDWARD A. DENNIS, RICHARD I. GILCHRIST, THEODORE D. ROTH, MARGARET FAYE WILSON, GREG N. LUBUSHKIN Defendants,	)	
-and-	)	
BIOMED REALTY TRUST, INC. Nominal Defendant.	)	

PLAINTIFF'S ANSWERING BRIEF IN OPPOSITION
TO THE INDIVIDUAL DEFENDANTS' AND NOMINAL DEFENDANT'S
MOTIONS TO DISMISS

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Other Authorities

I. NATURE AND STAGE OF PROCEEDINGS

Plaintiff Arnold Weinberg ("Plaintiff") respectfully submits this Answering Brief in Opposition to Defendants Alan D. Gold, Gary A. Kreitzer, Matthew G. McDivitt, R. Kent Griffin, Jr., Barbara R. Cambon, Edward A. Dennis, Richard I. Gilchrist, Theodore D. Roth, Margaret Faye Wilson and Greg N. Lubushkin's (the "Individual Defendants") and Nominal Defendant BioMed Realty Trust, Inc.'s ("BioMed" or the "Company") respective Motions to Dismiss.[1]

II. PRELIMINARY STATEMENT

A board of directors has an unwavering duty under Maryland law to act in the best interests of the corporation and its shareholders. Plaintiff's Complaint details well-pled facts demonstrating that BioMed's Board of Directors (the "Board") acted directly against the best interests of its shareholders and harmed the Company by approving, granting, and failing to rescind the Board's 2010 executive compensation plan through which the Board – despite its own stated pay-for-performance policy – gave large, undeserved pay hikes to the Company's top executives, amounting to a grossly excessive $10 million total compensation package, for a year in which BioMed's performance was abysmal.

BioMed's shareholders soundly rejected the Board's 2010 executive compensation plan, with more than 54% voting "against" these increased awards in the Company's first Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") mandated "say-on-pay"

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[1] In particular, this brief responds to the Memorandum of Law in Support of Individual Defendants' Motion to Dismiss Verified Shareholder Derivative Complaint, filed November 28, 2011 (D.I. 15) ("ID Br." or the Individual Defendants' "brief"), as well as to the Memorandum of Law in Support of Nominal Defendant BioMed Realty Trust, Inc.'s Motion to Dismiss Verified Shareholder Derivative Complaint, filed November 28, 2011 (D.I. 14) ("ND Br." or the Company's "brief").

vote on May 25, 2011, placing BioMed among one of only a tiny handful of companies (1.5%) to have its Board's executive compensation plan voted down by shareholders. This resounding "no" vote, combined with BioMed's terrible financial performance in 2010, is compelling evidence that the Board's granting of the big 2010 pay hikes was against the best interest of BioMed and its shareholders, and was thus in bad faith and in breach of its fiduciary duties of good faith and loyalty.

Since the shareholder vote, the Board has taken no action, nor indicated an intention to take any action, in response to the shareholders' plainly communicated expression of their own independent business judgment that the 2010 pay raises were unjustified and not in their best interests or BioMed's. Despite defying the will of the owners of the Company (its shareholder), the Individual Defendants nevertheless ask this Court to presume that they acted in the shareholders' best interests in granting and maintaining the 2010 pay hikes that the shareholders voted down. It simply makes no sense to apply such a presumption where, as here, the shareholders themselves have spoken (through a vote mandated by the Dodd-Frank Act and which is intended to "serve as a direct referendum on the decisions of the Compensation Committee" and allow shareholders "to stand up to excessively demanding officers"[2]), and

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[2] Dodd-Frank, S. Rpt. No. 111-176, 2010 WL 1796592, at 133, 231 (2010) ("shareowner votes on pay would serve as a direct referendum on the decisions of the compensation committee and would offer a more targeted way to signal shareowner discontent than withholding votes from committee members"); *see also id.* at 133 ("The Committee believes that shareholders, as the owners of the corporation, have a right to express their opinion collectively on the appropriateness of executive pay."). *Cf. IBS Fin. Corp. v. Seidman & Assocs., L.L.C.*, 136 F.3d 940, 949 (3d Cir. 1998) ("'[The shareholder franchise] is critical to the theory that legitimates the exercise of power by some (directors and officers) over vast aggregations of property that they do not own.'") (quoting *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 659 (Del. Ch. 1988)); *Mainiero v. Microbyx Corp.*, No. 14228-NC, 1996 Del. Ch. LEXIS 107, at *7-8 (Del. Ch. Aug. 15, 1996) ("Delaware Courts support the enfranchisement of Delaware's corporations'

expressed loud and clear that the 2010 pay raises are against their best interests. This is all the more true given that BioMed's shareholder base largely consists of sophisticated institutional investors who, through their extensive experience, are particularly well placed to exercise independent business judgment with respect to executive compensation.

Further, the Board's granting of the 2010 executive awards violated the Board's own executive compensation policy which, according to BioMed's Proxy Statement dated April 13, 2011 by which it solicited shareholders' approval of these awards (the "Proxy"), purportedly was designed "*to enhance BioMed's long-term financial performance and position, and thus stockholder value, by significantly aligning the financial interests of our executives with those of our stockholders*," achieve the "*aligning [of] our executive compensation structure with our stockholder's interests and market practices*," and ensure that "the executive compensation awarded by the compensation committee is dependent *in large part* on the compensation committee's assessment of *corporate performance and the executives' individual and business unit performance*...." Thus, the Proxy was materially false and misleading when made because it materially misrepresented that the Board's executive compensation policy was firmly rooted in a pay-for-performance philosophy, while failing to disclose that the 2010 executive compensation awards actually bore no meaningful relationship to the Company's performance.

While a board of directors is usually protected by the "business judgment rule" when making decisions about executive compensation, the business judgment rule is rebutted where, as here, a plaintiff alleges facts showing that board members acted in bad faith. Here, there should be no real dispute that the Board has deliberately acted against the shareholders in granting, and

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shareholders. The importance of allowing shareholders to vote at an annual meeting is critical to effective corporate governance.").

especially maintaining, the 2010 executive compensation awards, which the shareholder vote evidences were not in the best interest of BioMed or its shareholders. Indeed, the key facts confirming liability – all of which are well pled in the Complaint – are largely indisputable (and, in any event, must be taken as true at this stage). To wit, the essentially uncontestable facts show that: (i) BioMed's financial performance in 2010 was dismal, and, under the stewardship of the Individual Defendants, its stock has substantially underperformed the Company's peers and market as a whole over the last three years; (ii) the Board nevertheless awarded large compensation increases to top executives for 2010; (iii) the Board sought shareholder approval of the 2010 awards by way of a Proxy that (falsely) claimed that pay was directly tied to performance; (iv) the shareholders voted down the 2010 executive compensation plan by a substantial margin; and (v) the Board has failed to rescind the 2010 awards despite the shareholder vote against these awards.

The particularized facts set out in the Complaint, taken as true, rebut any presumption that the Board acted in shareholders' best interests when it approved and failed to rescind the undeserved 2010 pay hikes to top management. The Complaint demonstrates that: (i) the Board breached its fiduciary duties of loyalty and good faith by increasing 2010 executive pay in violation of the Board's stated pay-for-performance executive compensation policy and then refusing to take remedial action in response to the shareholder vote "against" these awards; (ii) the Board is not entitled to the business judgment presumption (and certainly not at the pleading stage); (iii) the executives who received the excessive 2010 awards were unjustly enriched at the expense of the Company by millions of dollars; (v) Defendants violated Section 14(a) and their fiduciary duty of candor by making the materially false and misleading statement that pay was

linked to performance, when it was not; and (vi) demand is excused because the Board has shown itself to be fully committed to its decision to maintain the excessive 2010 awards.

In response, Defendants largely rest on their erroneous contentions that Plaintiff should have made a pre-suit demand upon the Board and, in any event, the say-on-pay vote is advisory and therefore supposedly meaningless. Demand was not required because the Directors have shown themselves to be obviously committed to the $10 million pay package they gave, as they have taken no action, nor indicated they would take any action, in response to the shareholders' vote against these grossly excessive awards. It is obvious that a sole shareholder making a demand on this Board would have been a futile act where, as here, shareholders holding 64,441,624 shares – using their own independent business judgment as the owners of the Company – made a very public demand by voting against this excessive compensation, which demand the Board has ignored.

The advisory nature of the Dodd-Frank say-on-pay vote similarly provides Defendants no shelter, as contrary to Defendants' misinterpretation of the Complaint, this action is not about creating or implying any additional fiduciary duties for Defendants, but instead about enforcing their well-established duties of good faith and loyalty under Maryland law. The negative shareholder vote is certainly, at the very least, probative, if not the best evidence, that the 2010 executive compensation awards were not in the best interests of BioMed or its shareholders. It makes no sense to presume that the Directors acted in the best interests of the shareholders, when the shareholders themselves confirmed by a significant majority that – in their own business judgment as the owners of the Company – the Board's $10+ million increased pay package for the top executives for a year (2010) in which performance was terrible was not in best interests of the Company or its shareholders.

III. STATEMENT OF FACTS

BioMed describes its business as owning, acquiring, developing, redeveloping, leasing, and managing laboratory and office space for the life science industry. (¶ 27.)[3] BioMed's top management team includes the following Defendants: Gold, its Chief Executive Officer ("CEO"); Griffin, its President and Chief Operating Officer ("COO"); McDevitt, its Executive Vice President, Real Estate ("EVP"), and Lubushkin, its Chief Financial Officer ("CFO") (collectively, the "Executive Defendants"). (¶¶ 16-19.) Each of these Defendants was unjustly enriched as recipients of the excessive 2010 awards. In addition to CEO Gold (who, together with the rest of the Board, gave himself over $5 million for 2010, a raise of more than 23%), BioMed's Board consists of Defendants Kreitzer, Cambon, Dennis, Gilchrist, Roth, and Wilson. (¶¶ 19, 20-25.) Each of these Defendants acted disloyally and in bad faith in granting and failing to rescind the excessive 2010 awards, as well as by issuing (together with Defendants Gold, Griffin, McDevitt, and Lubushkin) a materially false and misleading proxy statement to the Company's shareholders (that also violated Section 14(a)).

A. BioMed's Dismal Financial Performance In 2010 and the Executives' Destruction of Stockholder Value Over The Last Three Years

BioMed has a record of underperformance under the stewardship of the Individual Defendants over the past several years, with a particularly dismal 2010 "performance". (¶¶ 5, 37-39.) As set forth in the Complaint, BioMed suffered, at the Individual Defendants' hands, substantial declines in net income, diluted earnings per share and cash dividend, and posted a negative cumulative three-year total stockholder return, trailing the positive three-year total stockholder return posted by BioMed's peers:

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[3] "¶__" and "¶¶__" refer to Plaintiff's Verified Shareholder Derivative Complaint, filed November 2, 2011 (the "Complaint").

- Net income declined from $60.19 million in 2009 to $39.31 million in 2010, a decrease of more than 34%;
- The Company's diluted earnings per share plunged from $0.45 in 2009 to $0.19 in 2010, a drop of more than 57%;
- The cash dividend to common stockholders fell from $0.70 to $0.63; and
- The Company posted a *negative* 3% cumulative three-year annual total stockholder "return", trailing the 9% cumulative three-year annual total stockholder return provided by the Company's peers and the 2.5% cumulative return posted by the MSCI US REIT Index (the "RMS").[4]

(¶¶ 5, 37-39.)

B. BioMed's Purported Performance-Based Executive Compensation Policy, The Grossly Excessive 2010 Executive Compensation Plan And Shareholders' Rejection Of That Plan

Like many publicly traded companies, BioMed's Board voluntarily chose to pay its executives (ostensibly) in accordance with a stated performance-based compensation policy. Here, the Board falsely represented to BioMed's shareholders – in recommending that the shareholders vote "for" the Board's 2010 executive compensation plan – that executive compensation was firmly rooted in a pay-for-performance philosophy. (¶¶ 7, 29-31, 91.) In particular, among the Board's materially false and misleading statements in the Proxy was that its executive compensation policy was designed "***to enhance BioMed's long-term financial performance and position, and thus stockholder value, by significantly aligning the financial interests of our executives with those of our stockholders,***" and to "promote individual accountability ***to deliver on t[the Company's] business objectives***" and achieve the "***aligning***

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[4] The RMS is a free float market capitalization weighted index that is comprised of Equity REIT securities that belong to the MSCI US Investable Market 2500 Index. The RMS represents the performance of the equity REIT investment opportunities set in the United States, which includes BioMed and many of its peers. (¶ 32, n. 4.)

[of] our executive compensation structure with our stockholder's interests and market practices." (¶¶ 7, 29-31.) Furthermore, the Board falsely stated that "the executive compensation awarded by the compensation committee is dependent ***in large part*** on the compensation committee's assessment of ***corporate performance and the executives' individual and business unit performance***...." (¶ 30.)[5]

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[5] Defendants improperly ask the Court to resolve their 12(b)(6) motions based on purported facts well beyond what is alleged in the Complaint, including particularly what the Board supposedly "actually considered in awarding the challenged compensation" (as drawn from the Board's self-serving characterizations in the Proxy). ID Br. at 3; *see also id.* at 4, n. 2; 8 (listing what, "[a]ccording to the Proxy Statement, the Compensation Committee evaluated"); 9 (claiming that "a number of factors actually considered by BioMed's Board in making executive compensation awards" are stated in the Proxy but not the Complaint); 19-20 (arguing based on purported "factors that the Compensation Committee considered"); Defendants' Request for Judicial Notice. While the Court may take judicial notice of and consider the fact that the Proxy (and 2010 Annual Report) were filed with the SEC and the words they contain, in doing so it may not, of course, accept the truth of what is stated therein. *See, e.g., It's My Party, Inc. v. Live Nation, Inc.*, No. JFM-09-547, 2012 WL 78795, *3 (D. Md. Jan. 10, 2012) ("Live Nation's motion must therefore be denied to the extent that Live Nation wants the facts of the exhibits to be judicially noticed for their truth; if any judicial notice is to be made of the exhibits, it must be limited to the fact that there were prior proceedings and prior filings. In other words, the exhibits may be judicially noticed not for the truth of the matters contained therein but merely to establish the fact of such prior proceedings if indeed that fact is relevant to establishing Live Nation's defense in this action."); *Moore v. Matthews*, 445 F. Supp. 2d 516, 528, n. 14 (D. Md. 2006) (declining to give judicial notice where defendant failed to establish that the proffered fact was "not subject to reasonable dispute") (quoting Fed. R. Evid. 201(b)).

Here, the Complaint references the Proxy not for its truth, but rather for the material misrepresentations allegedly contained therein. (¶¶ 7, 29-31, 91.) What the Compensation Committee actually did or did not consider in granting and failing to rescind the awards at issue are hotly disputed facts, and thus may not be established via judicial notice. *See id.*; *see also, e.g., Hennessy v. Penril Datacomm Networks*, 69 F.3d 1344, 1354-55 (7th Cir. 1995) (holding that district court properly refused to take judicial notice of a corporation's Form 10-K to determine a fact in dispute – the number of corporate employees); *Lovelace v. Software Spectrum*, 78 F.3d 1015, 1018 (5th Cir. 1996) (stating that SEC filings "should be considered only for the purpose of determining what statements the documents contain, not to prove the truth of the documents' contents); *In re Petco Animal Supplies Inc. Sec. Litig.*, No. 05-CV-0823-H, 2006 U.S. Dist. LEXIS 97927, at *6 (S.D. Cal. July 31, 2006) ("The district court must reject requests to the extent that parties seek to have the court accept as true the facts contained within public documents. Disputed factual questions are not suitable for judicial notice."); *Kramer v.*

The Board, contrary to its fiduciary responsibilities and own stated executive compensation policy, unreasonably gave exorbitant executive compensation and granted large, undeserved pay hikes to the Company's top executives despite the Company's and Executive Defendants' *underperformance*. This manifest underperformance included the Executive Defendants' evisceration of the Company's net income and diluted earnings per share, in addition to their record of failure in posting a *negative* cumulative three year annual return for the Company's shareholders when its peers, and the RMS as a whole, were posting positive returns for shareholders in the same period. (¶ 32.) Because of their high-level positions and access to BioMed's internal information, Defendants must have known that granting the excessive 2010 executive compensation while BioMed's financial performance declined violated the Board's stated pay-for-performance executive compensation policy as outlined in the Proxy disseminated to shareholders. (¶ 52.)

Despite BioMed's terrible performance under the Individual Defendants, the Board inexplicably granted substantial, unearned compensation *increases* to the Company's top executives for 2010, for a total pay package of more than $10 million -- a hike of nearly $28%. (¶¶ 36, 41.) Specifically:

- Gold's pay as CEO was raised sharply, to $5,032,814 in 2010 from $4,071,814 to in 2009 to, an increase of more than 23% (¶¶ 16, 36);

- Griffin's pay as President and COO was increased substantially, to $2,782,962 in 2010 from $2,275,899 in 2009, a rise of more than 22% (¶¶ 17, 36); and

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Time Warner, Inc., 937 F.2d 767, 774 (2d Cir. 1991); 15 U.S.C. § 78z; 17 C.F.R. § 240.14c-6(b). Notably, *Jacobs Engineering Group, Inc. Consol. S'holder Deriv. Litig.*, No. 4-11-cv-02537 (Los Angeles Super. Ct. Nov. 10, 2011) – one of the documents that Defendants ask the Court to take judicial notice of – held, under analogous California evidentiary standards, that "judicial notice of the exhibits should be limited to the fact that these items are filings with the SEC. The Court should not judicially notice the truth of these exhibits." Declaration of J. Christian Word, Ex. 6, at 2.

- McDevitt's pay as EVP was boosted to $2,321,899 in 2010 from $1,597,833 in 2009, an increase of more than 45% (¶¶ 18, 36).

In addition, Lubushkin who has served as CFO of BioMed since May 2010 was granted an extraordinarily generous and undeserved $802,166 in total compensation for 2010. (¶¶ 19, 37.)

Moreover, because the Board provided grossly excessive executive compensation untethered to corporate performance to the Company's top executives, the Board was consequently unable to issue a plan under Internal Revenue Code § 162(m), and thus further harmed BioMed by failing to take advantage of substantial corporate tax deductions that are available when, unlike here, executive compensation is actually tied to the achievement of corporate performance-based goals. (¶ 40.)

On May 25, 2011, BioMed's shareholders soundly rejected the Board's 2010 executive compensation plan – using their own independent business judgment as the owners of the Company – with more than 54% voting "against" these increased awards at the Company's Dodd-Frank Act mandated say-on-pay vote, placing BioMed as one of only a tiny handful of companies to have its Board's executive compensation plan voted down by shareholders under the Dodd-Frank Act. (¶¶ 4, 43.) In particular, 64,441,624 votes were cast "against" the Board's 2010 executive compensation program, with only 54,369,424 votes "for" it, according to the Form 8-k filed by the Company with the SEC on June 1, 2011. (¶ 44.) Notably, sophisticated institutional investors hold at least 31%, and likely as much as 93%, of BioMed's voting shares, including among others, BlackRock, Inc., Columbia Wanger Asset Management, LLC, LaSalle Investment Management L.P., and The Vanguard Group, Inc. (¶¶ 4, 8. 43.) Such institutional investors are particularly well placed to exercise independent business judgment with respect to executive compensation. (*Id.*)

The sophisticated institutional shareholders and the Company's other stockholders used their own independent business judgment, in their capacity as the owners of the Company, to flatly reject the Board's exorbitant pay hikes for executives who have done little more than destroy long-term stockholder value and weaken the Company's financial position. (¶¶ 4, 36-39, 41.) Nevertheless, the Board has wrongly failed to rescind these awards, and the top executives still unjustly retain them.

Although the adverse shareholder vote (and Defendants' bad faith) rebut any presumption that the Board's 2010 executive compensation decisions were the product of a valid exercise of business judgment (as the Board should not be presumed to have acted in the shareholders' best interests in granting and maintaining the exorbitant 2010 pay package when the shareholders themselves confirmed that it was against their best interests) the Board has wrongly failed to rescind or otherwise modify the excessive 2010 executive compensation, nor has it publicly indicated any intention to do so. (¶¶ 7, 46.) The Board has inexplicably remained silent regarding the say-on-pay vote rejecting the 2010 executive compensation, thus ignoring the will of BioMed's shareholders despite the Board's (false) statement in the Proxy that it purportedly "value[s] the opinion of the stockholders." (*Id.*)

The Board plainly has shown itself to be obviously committed to maintaining the grossly excessive 2010 executive compensation, thus excusing demand, by first recommending that the shareholders approve the excessive 2010 compensation, and then thwarting the will of the shareholders in failing to rescind or otherwise modify these massive awards despite the shareholders' public demand that they do so through their decisive vote against this undeserved pay. (¶¶ 66, 82.)

The executives still unjustly retain the money, despite knowing that they are not entitled to it, including CEO and Chairman of the Board Gold, to whom his Board of Directors granted to himself and his top executive team this massive increased $10 million pay package, notwithstanding the Company's dismal "performance" and the contravention of the Board's stated pay-for-performance policy represented to the shareholders. (¶¶ 16, 84.) Further, Gold and the rest of the Board, to this day, have continued to maintain the grossly excessive 2010 pay, in utter disregard of the decisive shareholder vote confirming that it was not in the shareholders' or Company's best interests. (*Id*.)

IV. **LEGAL STANDARD**

"In ruling on a motion to dismiss, the factual allegations in the plaintiff's complaint must be accepted as true and those facts must be construed in the light most favorable to the plaintiff." *Atlantic Forest Products LLC v. Wm. M. Young Co. LLC*, No. RDB-11-0241, 2011 WL 6351851, *1 (D. Md. Dec. 19, 2011) (citing *Edwards v. City of Goldsboro*, 178 F.3d 231, 244 (4th Cir. 1999)). Because "'the purpose of Rule 12(b)(6) is to test the sufficiency of a complaint and not to resolve contests surrounding the facts, the merits of a claim, or the applicability of defenses,'" *Atlantic Forest*, 2011 WL 6351851 at *1 (quoting *Presley v. City of Charlottesville*, 464 F.3d 480, 483 (4th Cir. 2006)), "'[w]hen ruling on such a motion, the court must "accept the well-pled allegations of the complaint as true,'" and "'construe the facts and reasonable inferences derived therefrom in the light most favorable to the plaintiff,'" *id.* at *2 (quoting *Ibarra v. United States*, 120 F.3d 472, 474 (4th Cir. 1997)). "In sum, if a complaint 'pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged,' then the complaint is 'plausible on its face,' and will survive a motion to dismiss under Rule 12(b)(6)." *Dutton v. Harris Stratex Networks*, 270 F.R.D. 171, 175 (D. Del. 2010) (citing *Ashcroft v. Iqbal*, 556 U.S. 662, 129 S.Ct. 1937, 1949 (2009)).

"[D]ismissal is inappropriate unless, accepting as true the well-pled facts in the complaint and viewing them in the light most favorable to the plaintiff, the plaintiff is unable to 'state a claim to relief that is plausible on its face.'" *Brockington v. Boykins*, 637 F.3d 503, 505-06 (4th Cir. 2011) (quoting *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 570 (2007) (directing that the factual allegations of a complaint are to be taken "as a whole" in determining whether they state a facially plausible claim to relief)). "The plausibility standard requires that the pleader show more than a sheer possibility of success, although it does not impose a 'probability requirement.'" *Atlantic Forest*, 2011 WL 6351851 at *2 (quoting *Twombly*, 550 U.S. at 556). "Instead, '[a] claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged.'" *Id.* (quoting *Iqbal*, 129 S. Ct. at 1949 (2009)). "Thus, a court must 'draw on its judicial experience and common sense' to determine whether the pleader has stated a plausible claim for relief. *Id.* (quoting *Iqbal*, 129 S. Ct. at 1950).

V. ARGUMENT

A. Plaintiff Has Stated A Claim For Breach Of Fiduciary Duty

1. Plaintiff Has Alleged Facts Sufficient To Rebut Any Business Judgment Rule Presumption Regarding The Excessive 2010 Executive Pay

"It has long been established . . . that directors of Maryland corporations stand in a fiduciary relationship to the corporations they manage and the shareholders of those corporations, a relationship that imposes on directors duties of care, loyalty, and good faith." *Shenker v. Laureate Educ., Inc.*, 983 A.2d 408, 420 (Md. 2009) (citing *Hoffman Steam Coal Co. v. Cumberland Coal & Iron Co.*, 16 Md. 456, 507 (1860); *Booth v. Robinson*, 55 Md. 419 (1881); *Storetrax.com, Inc. v. Gurland*, 915 A.2d 991, 1000 (Md. 2007); *Mona v. Mona Elec. Group, Inc.*, 934 A.2d 450, 463 (Md. Ct. Spec. App. 2007)). Further, Directors have the

fiduciary duty to act in a manner they reasonably believe to be in the best interests of the corporation and its shareholders. *See, e.g.*, *Indurated Concrete Corp. v. Abbott*, 74 A.2d 17 (1950); *Rosenbloom v. Electric Motor Repair Co.,* 358 A.2d 617 (1976); Md. Corps. & Ass'ns Code § 2-405.1(a)(2). In addition, "officers and directors of a corporation stand in a sufficiently confidential relation to the corporation's stockholders to impose a duty upon them to reveal all facts material to corporate transactions." *Shenker*, 983 A.2d at 338 (quoting *Parish v. Maryland & Virginia Milk Producers Ass'n*, 242 A.2d 512, 539 (1968)).

"These fiduciary duties are not intermittent or occasional, but instead are the 'constant compass by which all director actions for the corporation and interactions with its shareholders must be guided.'" *Shenker*, 983 A.2d at 338 (quoting *Storetrax*, 915 A.2d at 1001; *Malone v. Brincat*, 722 A.2d 5, 10 (Del. 1998)). The "confidence reposed in [directors], and the position they occupy towards the corporation and its stockholders, require a strict and faithful discharge of duty". *Shenker*, 983 A.2d at 338 (quoting *Booth*, 55 Md. at 437; *Coffman v. Maryland Publ'g Co.*, 173 A. 248, 254 (1934)).[6]

The Individual Defendants' central argument in seeking to escape the clear-cut breach of fiduciary demonstrated by the facts alleged in the Complaint is that they purportedly should be *presumed* by this Court to have "acted in good faith and in best interests of the corporation" and its shareholders (ID Br. at 11; *see also id.* at 2, 10-18) in granting and failing to rescind the 2010

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[6] Delaware law is in accord. *See, e.g.*, *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 360 (Del. 1993) ("In exercising these powers, directors are charged with an unyielding fiduciary duty to protect the interests of the corporation and to act in the best interests of its shareholders"), *decision modified on reargument on other grounds*, 636 A.2d 956 (Del. 1994); *In re Tyson Foods, Inc.*, Civ. A. No. 1106-CC, 2007 WL 2351071, at *4 (Del. Ch. Aug. 15, 2007) (directors and officers have a duty of "unremitting loyalty"; "Loyalty. Good faith. Independence. Candor. These are words pregnant with obligation. The Supreme Court did not adorn them with half-hearted adjectives. Directors should not take a seat at the board table prepared to offer only conditional loyalty, tolerable good faith, reasonable disinterest or formalistic candor.").

pay hikes, despite the loudly expressed view of a sizable majority the shareholders themselves – through a legally mandated vote – that, as determined in their own independent business judgment as the owners of the Company (and thus of the money being given away), these excessive grants were not in their best interests.

As Defendants acknowledge, the business judgment rule does not shelter directors from liability where, as here, the facts alleged show they acted in bad faith. ID Br. at 11 (citing *NAACP v. Golding*, 679 A.2d 554, 559 (Md. 1996); *Black v. Fox Hills N. Cmty. Ass'n, Inc.*, 599 A.2d 1228 (Md. Ct. App. 1992)). *See Daniels v. New Germany Fund, Inc.*, No. MJG-05-1890, 2006 WL 4523622, *3 (D. Md. Mar. 29, 2006) ("Defendants seek to shield themselves from suit by virtue of the Business Judgment Rule. However, they ignore the circumstance that, in a dismissal context, the Court must accept Plaintiffs' pleadings. In the instant case, Plaintiffs have alleged bad faith – a fact that, if proven, strips the protection of the Business Judgment Rule.").

Here, the Complaint more than sufficiently alleges facts demonstrating the Individual Defendants' bad faith. These facts are set out in the largely indisputable particularized factual allegations of the Complaint, including the adverse shareholder vote – which will always reflect the shareholders' determination that the 2010 pay was not in their best interests – as well as the documented facts of the Company's dismal performance under the stewardship of the Individual Defendants,[7] the massive pay hikes themselves, and the Defendants' allegedly false and misleading statements to shareholders in recommending that the shareholders approve the excessive 2010 pay plan. In short, the Complaint "plead[s] facts sufficient to rebut the business

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[7] Plaintiff does not merely "disagree[]" with the Board's evaluation of performance (ID Br. at 3, 14), but rather submits that the "performance" detailed in the Complaint was objectively terrible. Defendants' attempt to introduce new purported facts (such as different metrics) may not be countenanced at this stage. *See supra*, at 8, n. 5.

judgment rule under Maryland law." (ID Br. at 14; *see also id.* at 12 (acknowledging that where the "particular allegations that the Board's determinations regarding executive compensation were . . .made in bad faith, the Business Judgment rule is . . . rebutted).

a. The Adverse Shareholder Vote And The Board's Bad Faith Granting and Failing To Rescind The Excessive 2010 Executive Pay Rebut Any Presumption Of Business Judgment.

Defendants baldly submit, without citation, that the shareholders' decisive rejection of the 2010 pay hikes should have "no impact whatsoever upon the standards by which the Board's conduct is reviewed, nor upon the validity of the Board's compensation decisions before or after the [say-on-pay] vote." ID Br. at 17-18 (citing nothing and generally referencing the "plain language of Dodd-Frank"). That is not the law, nor what the law should be.

In particular, Defendants baselessly rely upon the undisputed fact that the Dodd-Frank Act provides that a negative say-on-pay vote is advisory and does not, *inter alia*, "create or imply any change to the [Board's] fiduciary duties," "create or imply any change additional fiduciary duties," or "overrul[e] a decision by [the Board]" (ID Br. at 15-16 (citing 15 U.S.C. 78n-1(c)); *see also id.* at 1). Plaintiff, however, does <u>not</u> contend that the shareholders' rejection of the 2010 pay raises does any of these things, or otherwise "change[s] or augment[s]" the Board's fiduciary duties in any way or "create[s] or impl[ies] any additional fiduciary duties" or otherwise binds the Board to take a particular action (*id.* at 1, 15-16). Rather, the shareholders' rejection of the increased pay package granted by the Board has two key effects here. First, it is powerful evidence that the Directors in fact breached their existing, well-established fiduciary duties of good faith and loyalty under Maryland law by not acting in the best interests of the Company and its shareholders. Second, it confirms that the Directors are not entitled to the business judgment rule presumption that – in directly contravening the expressed will of the shareholders – they supposedly acted "in good faith and in the best interests of the corporation."

ID Br. at 11 (quoting *Wittman v. Crooke,* 707 A.2d 422, 425 (Md. Ct. App. 1992)).[8]

These two effects of the negative say-on-pay vote are perfectly logical and consistent with the Dodd-Frank Act and Maryland and Delaware law (which Maryland courts look to in matters of corporate governance such as those at issue here).[9] The vote is strong evidence that the Board breached its fiduciary duties because shareholders holding more than *64 million shares*, or 54% of BioMed common stock (many of whom are sophisticated institutional investors), voted against the Board's plan, determining in their independent business judgment – as the owners of the Company – that the increased awards were not in their best interests or those of the Company, and yet the Board has not acted to rescind or otherwise modify the excessive compensation. In light of this referendum, the Board's subsequent decision to keep the 2010 executive compensation in place only reinforces that the Board's actions were in bad faith (and

[8] Unlike here, in *Wittman*, there was "simply *no evidence* that [the directors] failed to act in good faith" (and thus it made sense there to "'presum[e] th[e] directors . . . acted in good faith and in the best interests of the corporation'"). *Id.*, 707 A.2d at 425 (emphasis added) (citing *Zimmerman v. Bell*, 800 F.2d 386, 392 (4th Cir. 1986) (applying Maryland law)). *See also* ID Br. at 14 (quoting *Prod. Res. Group, L.L.C. v. NCT Grp., Inc.*, 863 A.2d 772, 799 (Del. Ch. 2004) ("The fact that [executives] received substantial salaries during a period when [the company] was performing poorly would not, *without more*, ordinarily sustain a claim.") (alteration in Defendants' brief; emphasis added). Here, far from there being "no evidence" or nothing "more", the shareholder say-on-pay vote powerfully evidences that the Board's 2010 pay package was not in the Company's or their best interests, as determined by the Company's owners (the shareholders) using their own independent business judgment. This evidence is all the more powerful because sophisticated institutional investors make up a large part of the Company's shareholder base, and such institutional investors are particularly well placed to exercise independent business judgment with respect to executive compensation. (*See* ¶¶ 4, 8, 43.) Further, there is "more", including the Board's materially false and misleading statements to the shareholders regarding its 2010 executive compensation program, which further demonstrate the Individual Defendants' bad faith.

[9] *See* ID Br. at 13, n. 4.

that the Board is fully committed to its decision to maintain the 2010 pay packages, thus excusing demand (*see infra*, § V.E)).[10]

Here, the Individual Defendants' bad faith is apparent, given the decisive rejection by the shareholders of the 2010 executive awards strongly evidences that this pay is not in the best interest of BioMed or its shareholders (¶ 53), as well as because, given the Individual Defendants' high-level positions and access to BioMed's internal information, they must have known that granting the excessive 2010 executive compensation while BioMed's financial performance declined substantially violated the Board's stated pay-for-performance executive compensation policy (¶ 52). Further, Defendants solicited the shareholders to vote "for" their excessive 2010 pay plan by way of a Proxy that was materially false and misleading when made, in that it misrepresented that executive compensation was supposedly tied meaningfully to performance, while wrongly failing to disclose that the 2010 executive compensation violated the Board's own stated performance-based executive compensation policy and actually bore no meaningful relationship to corporate performance. (¶ 55.)

Further, directors who act, as here, directly against the expressed will and judgment of the owners of the corporation as expressed in a legally required shareholder vote are not entitled to a presumption that they acted in the best interests of the corporation and its owners. At

[10] That the Board has breached its fiduciary duty and acted in bad faith is further evident from the materially false disclosures it made in the 2011 Proxy Statement regarding executive compensation. *See*, *e.g*., *Shenker*, 983 A.2d at 338 ("officers and directors of a corporation stand in a sufficiently confidential relation to the corporation's stockholders to impose a duty upon them to reveal all facts material to corporate transactions") (quoting *Parish v. Maryland & Virginia Milk Producers Ass'n*, 242 A.2d 512, 539 (1968)); *cf. In re INFOUSA, Inc. Shareholders Litig.*, 953 A.2d 963, 990 (Del. Ch. 2007) ("shareholders are entitled to honest communication from directors, given with complete candor and in good faith"). Departure from this responsibility violates the fiduciary duties that protect shareholders, and such violations are sufficient to subject directors to liability in a derivative claim for harm caused to the corporation. *See infra*, at 33, n. 25.

bottom, it simply does not make sense to presume that the Directors exercised good faith business judgment where, as here, the shareholders' unequivocally rejected the Board's executive compensation plan, demonstrating that *many* reasonable persons (who own the Company) doubted the propriety of the Board's decision and rejected it outright. In making and adhering to a decision so at odds with the expressed will of a clear majority of the Company's shareholders (many of whom are sophisticated institutional investors), the Directors should not be presumed to have acted in good faith and in the best interests of the Company and its shareholders.

Indeed, Delaware law (which the Court may be guided by here[11]) has long held that, in appropriate circumstances, directors are not entitled to the business judgment rule's deference when the directors' actions or inactions are contrary to a vote of the shareholders. *See*, *e.g.*, *In re John Q. Hammons Hotels Inc. S'holder Litig.*, No. 758-CC, 2009 WL 3165613, at *12 (Del. Ch. Oct. 2, 2009) (holding that given "deficiencies in the specific procedures used" the business judgment rule would apply only "if the transactions were (1) recommended by a disinterested and independent special committee, *and* (2) approved by stockholders in a non-waivable vote of the majority of all the minority stockholders") (emphasis in original); *In re Wheelabrator Techs., Inc. S'holders Litig.*, 663 A.2d 1194, 1202-3 (Del. Ch. 1995) ("[T]he ratification cases involving duty of loyalty claims have uniformly held that the effect of shareholder ratification is to alter the standard of review, *or* to shift the burden of proof, *or* both.") (emphasis in original)). The Directors' disloyal behavior here in maintaining excessive levels of compensation – despite the fact that a substantial majority of BioMed's shareholders expressly rejected these awards –

[11] *See* ID Br. at 13, n. 4.

likewise should alter the standard of review from the deference of business judgment to the scrutiny of entire fairness, and shift the burden of proof to the Directors (to show that the awards were entirely fair to the Company). *See, e.g., Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1162 (Del. 1995) (once business judgment rule rebutted burden shifts to defendants to prove entire fairness).[12]

Thus, while the Company may not be obligated to accept or implement the shareholders'

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[12] To be perfectly clear, Plaintiff does not claim that a negative say-on-pay vote equates to a *per se* breach of fiduciary duty or that it is conclusive evidence that the Board breached its duties. Rather, Plaintiff submits that the negative say-on-pay vote, and the Board's failure to take corrective act in response to it, removes any presumption that the Directors behaved in good faith and in the best interests of the Company and its shareholders. Defendants remain free, of course, to attempt to prove at trial that the challenged compensation was entirely fair. That will, however, be quite difficult for Defendants to do, given not only the negative shareholder vote, but also the Company's dismal performance under the stewardship of the top executives to whom the Board gave the allegedly excessive and undeserved payments.

Defendants are highly likely to fail to meet their burden of proof at summary judgment and trial, given that the result of the shareholder vote cannot be undone. The adverse say-on-pay vote will always reflect the fact that BioMed's shareholders determined, in their own independent business judgment as the owners of the Company, that the 2010 executive compensation plan was not in their best interests. This is compelling evidence that the Board breached its duty of good faith by acting against the best interests of shareholders when giving and maintaining the 2010 executive pay raises.

The cases cited by Defendants are inapposite because they did not even involve a stockholder vote. For example, *In re The Goldman Sachs Group, Inc.*, No. 5215-VCG, 2011 WL 4826104 (Del. Ch. Oct. 12, 2011) (cited by the Individual Defendants at page 13 of their brief), involved a general challenge to Goldman's compensation structure in that the Goldman board based compensation on a percentage of net revenue, which allegedly gave its employees an improper "motivation to grow net revenue at any cost regardless of risk." *Id.* at *1. Here, in contrast, BioMed's shareholders voted – in a vote mandated by the Dodd-Frank Act – and decisively rejected the Board's executive compensation structure; yet, the Board has continued to disregard the shareholders' will (and determination of their own best interests). The Board simply should not be *presumed* to have acted in good faith and in the shareholders' best interests when it has acted directly against the expressed will and determination of the majority of the Company's shareholders as expressed in a legally mandated vote that is intended to be a "direct referendum" on the Board's decision. S. Rep. No. 111-176, 2010 WL 1796592, at 231.

views regarding the excessiveness of the compensation grants at issue, the Directors' utter disregard of the shareholders' views (as expressed by their decisive defeat of the Board's 2010 executive pay plan) should remove any presumption that in doing so the Directors complied with their well-settled fiduciary duties under Maryland law. Indeed, the vote – whether advisory or not – reflects the will of the shareholders and is direct evidence that the 2010 pay raises were not in their best interests. *See, e.g.*, *Gantler v. Stephens*, 965 A.2d 695, 713 (Del. 2009) (stating that even non-legally binding shareholder votes can have dispositive effect).

Notably, the Senate Banking Report confirms that the purpose of the say-on-pay vote is to provide an efficient means for shareholders, as the owners, to collectively express whether the corporation's executive compensation is in their best interests as shareholders. S. Rep. No. 111-176, 2010 WL 1796592, at 133 (2010) ("The Committee believes that shareholders, as the owners of the corporation, have a right to express their opinion collectively on the appropriateness of executive pay."; the say-on-pay vote is to allow shareholders "to stand up to excessively demanding officers"); *id.* at 231 ("shareowner votes on pay would serve as a direct referendum on the decisions of the compensation committee and would offer a more targeted way to signal shareowner discontent than withholding votes from committee members").[13] Given the Dodd-Frank Act, courts now have a mechanism to objectively determine whether executive compensation is in the best interests of shareholders. Courts no longer need to rely

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[13] *See also* ¶ 3. *Cf., e.g.*, *IBS Fin. Corp. v. Seidman & Assocs., L.L.C.*, 136 F.3d 940, 949 (3d Cir. 1998) ("'[The shareholder franchise] is critical to the theory that legitimates the exercise of power by some (directors and officers) over vast aggregations of property that they do not own.'") (quoting *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 659 (Del. Ch. 1988)); *Mainiero v. Microbyx Corp.*, No. 14228-NC, 1996 Del. Ch. LEXIS 107, at *7-8 (Del. Ch. Aug. 15, 1996) ("Delaware Courts support the enfranchisement of Delaware's corporations' shareholders. The importance of allowing shareholders to vote at an annual meeting is critical to effective corporate governance.").

heavily on process-oriented factors to try to discern whether executive compensation serves the best interests of shareholders. *See infra*, at 25, n. 19 (discussing *In re Walt Disney*, 907 A.2d at 697 (recognizing that under modern principles of corporate governance the Disney Board's decision to pay Ovitz many millions might well not withstand scrutiny under the business judgment rule)). Now, courts may simply examine the results of the say-on-pay votes to determine whether shareholders, in their own independent business judgment, view the executive compensation as in their best interests as owners.

Further supporting the viability of Plaintiff's claims is the pertinent recent decision in *NECA-IBEW Pension Fund v. Cox*, C.A. No. 1:11-cv-451, 2011 WL 4383368, (S.D. Ohio Sept. 20, 2011) ("*Cox*"),[14] which Defendants barely mention in their briefing. *Cox* is a "say-on-pay" derivative case similar to the instant litigation, where the Court upheld claims like those at bar. The Court held that the "Cincinnati Bell's Board is not entitled to business judgment protection for its 2010 executive pay hikes" because the factual allegations made there – which are akin to those in Plaintiff's Complaint – "raise a plausible claim that the multi-million dollar bonuses approved by the directors in a time of the company's declining financial performance violated Cincinnati Bell's pay-for-performance compensation policy and were not in the best interests of Cincinnati Bell's shareholders and therefore constituted an abuse of discretion and/or bad faith." 2011 WL 4383368, *3 (footnotes omitted).

The Court further held (in excusing demand as futile under Ohio law) that the "plaintiff has pled specific facts to give reason to doubt that the directors could make unbiased,

[14] The *Cox* decision is attached as Exhibit A to the Declaration of Michael H. Rosner, Esq., dated January 16, 2012, and submitted herewith (the "Rosner Declaration").

independent business judgments about whether to sue." *Id.* at *4. In reasoning directly applicable to the fiduciary duty claims here, the Court found:

> The director defendants are the very same people who approved the pay hikes and bonuses, and plaintiff has named all directors who approved the compensation as defendants. Moreover, in this case, *the directors did not merely approve the transaction, they also recommended to the shareholders that the shareholders approve the compensation. Given that the director defendants devised the challenged compensation, approved the compensation, recommended shareholder approval of the compensation, and suffered a negative shareholder vote on the compensation*, plaintiff has demonstrated sufficient facts to show that there is reason to doubt these same directors could exercise their independent business judgment over whether to bring suit against themselves for breach of fiduciary duty in awarding the challenged compensation. The Court concludes, at the dismissal stage, that plaintiff's allegations create a reasonable doubt that the challenged transaction is the result of a valid business judgment, and, accordingly, the directors possess a disqualifying interest sufficient to render pre-suit demand futile and hence unnecessary.

Id. (footnote omitted; emphasis added).

Given that *Cox* is on all fours with this case, Defendants cursorily assert that it is inapposite because Ohio law governed there, and that Ohio law purportedly "does not require a plaintiff to plead facts rebutting the business judgment rule." ID Br. at 17, n. 6. That in no way undermines the applicability of *Cox* to this case, as the Court expressly found that the complaint there "provides factual allegations and not simply conclusory allegations" and that "[t]hese factual allegations raise a plausible claim that the multi-million dollar bonuses approved by the directors in a time of the company's declining financial performance violated Cincinnati Bell's pay-for-performance compensation policy and were not in the best interests of Cincinnati Bell's shareholders and therefore constituted an abuse of discretion and/or bad faith." *Id.* at *3

(footnotes omitted).[15] These findings were based upon core factual allegations (*i.e.*, large executive pay raises, negative corporate financial performance metrics, adverse say-on-pay vote, and a purported pay-for-performance policy that was allegedly violated) that are likewise at the heart of Plaintiff's Complaint in the instant litigation. *See id.*[16]

Defendants also pin their hopes on an unreported decision from a case in Georgia state court—*Teamsters Local 237 Additional Security Benefit Fund v. McCarthy*, No. 2011-cv-197841 (Ga. Super. Ct. Sept. 16, 2011) (slip op.) ("*McCarthy*"). *McCarthy* is starkly different to the case at bar.[17] Unlike here, the board of directors in *McCarthy* actually adhered to the compensation policy which had been established and communicated to shareholders. *Id.* at 5 ("The allegations in Plaintiffs' complaint neither contradict any part of that sequence of events (concerning the award of executive compensation) nor in any way suggest that the challenged 2010 executive compensation was not paid in accordance with the pre-established performance goals and the terms of the [company's incentive plan]."). The court's reasoning, therefore, relied solely on the plaintiffs' conclusory allegations that the board had awarded excess pay in accordance with previously established yet unchallenged objectives, *see id.* at 9-10, and disregarded the outcome

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[15] Like Maryland, Ohio's business judgment rule does not shield directors where they act in bad faith. *See id.* at *2. As discussed below, demand is excused in the instant case because the directors have shown themselves to be committed to the 2010 executive pay hikes. *See infra*, § V.E.

[16] The only other attack that the Individual Defendants make on *Cox* is that the Los Angeles Superior Court did not find it to be "persuasive" in *Jacobs Engineering Group, Inc. Consol. S'holder Deriv. Litig.*, No. 4-11-cv-02537 (Los Angeles Super. Ct. Nov. 10, 2011). ID Br. at 17, n. 6. *Jacobs*, however, is itself unpersuasive, as that court did not support its conclusion with any reasoning.

[17] As an preliminary matter, the court in *McCarthy* had made an initial finding that the plaintiffs lacked standing because they did not hold stock when the board's alleged misconduct began. *McCarthy*, slip op. at 5-6. Accordingly, the remainder of the court's opinion, including that which assessed the sufficiency of plaintiffs' demand futility allegations, was pure *dicta*.

of the shareholder vote, *see id.* at 10-13. By contrast, Plaintiff here alleges, among other things, that BioMed's Board purported to establish, but then blatantly disregarded, its stated "pay-for-performance" scheme for awarding the Company's senior executives. *McCarthy* is, therefore, unavailing and should be limited to its facts.[18]

b. The Board Exceeded Its Discretion With Respect To The Excessive 2010 Executive Pay

Defendants acknowledge that particular allegations that the Board's determinations regarding executive compensation were made in bad faith rebut the business judgment rule, and, in any event, the Board does not have unlimited discretion in setting executive compensation. *See* ID Br. at 12. Indeed, as Defendants' own citation recognizes, "there is an outer limit to that discretion." *Brehm v. Eisner*, 746 A.2d 244, 262 (Del. 2000).[19] Here, well beyond any reasonable or rational discretion, the Board awarded huge executive pay increases despite not

[18] To the extent that it constitutes any authority at all, *McCarthy* does nothing more than suggest that a non-binding shareholder vote does not *alone* suffice to rebut the presumption of the business judgment rule with respect to compensation decisions. *See id.* at 16. Here, however, Plaintiff's Complaint alleges far more than just the negative shareholder vote, including the Board's establishment of performance-based policy for rewarding executives, the Board's misrepresentations to shareholders that it would follow this stated policy, and the Board's blatant disregard of the policy and their representations to shareholders concerning it. In any event, Plaintiffs submit that *McCarthy* was wrongly decided and that the reasoning of *Cox* is more convincing.

[19] Defendants' reliance upon *Brehm* is misplaced. (ID Br. at 12 (quoting *Bender v. Schwartz*, 917 A.2d 142, 161 (Md. Ct. App. 2007) (quoting *Brehm*, 746 A.2d at 263)). In *Brehm* (and in the other cases Defendants cite here), the executive compensation was never subject to a shareholder vote, let alone rejected, as was the case here. Further, *Brehm* survived both dismissal and summary judgment motions, and proceeded to trial. At trial, although the Court ultimately ruled against plaintiffs, the Court noted that its decision may have been different if the compensation was granted in "an era that has included the Enron and Worldcom debacles, and the resulting legislative focus on corporate governance." *In re Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 697 (Del. Ch. 2005), *aff'd*, 906 A.2d 27 (Del. 2006). With the enactment of Dodd-Frank, we now live in such an era, requiring a different result here.

only abysmal performance but also shareholders' own business judgment (as loudly expressed by their vote) that the 2010 raises were not in the best interests of the Company or its shareholders.

The other cases Defendants cite – none of which involved a shareholder vote on the compensation at issue – likewise do not preclude Plaintiff's well-pled claims. *See* ID Br. at 12-13. In *Mona v. Mona Elec. Group, Inc.*, 934 A.2d 450 (Md. Ct. Spec. App. 2007), the case proceeded to trial but the Court granted a motion for judgment because the plaintiff had adduced "no evidence . . . that the judgments made by the Board of Directors . . . were anything other than in good faith," and "it was incumbent upon [the plaintiff] to adduce some evidence to rebut the presumption that, in setting [executive] compensation . . . the directors acted in good faith and in a manner they reasonably believed was in the best interest of the corporation." *Id.* at 466. Here, although still at the pleading stage, Plaintiff has plainly adduced at least "some evidence to rebut the presumption that . . . the directors acted in good faith and in a manner they reasonably believed was in the best interest of the corporation" – including the negative shareholder vote, the Company's poor performance under the leadership of the Executive Defendants, and the Board's violation of its own stated pay-for-performance policy.[20]

Further, where, as here, a board adopts a particular executive compensation policy, the directors are obligated to adhere to the terms of their policy. *See, e.g., Ryan v. Gifford,* 918 A.2d 341, 357 (Del. Ch. 2007) (directors acted disloyally by retroactively selecting price for options

[20] Nor is *McQuillen v. National Cash Register Co.*, 27 F. Supp. 639 (D. Md. 1939), of any help to Defendants. There, the Court recognized that the business judgment rule does not protect directors' compensation decisions unless "they acted in good faith within their powers, and the salaries fixed by them were not clearly excessive." *Id.* at 651 (quoting *Matthews v. Headley Chocolate Co.*, 130 Md. 523, 535, 100 A.2d 645, 650 (1917)). The *McQuillen* Court further observed that executive pay may be "so exorbitant as to preclude a finding of good faith". *Id.* at 652.

being granted to executives when their option-granting policy required the price to be set on the date of the grant); *Weiss v. Swanson*, 948 A.2d 433, 437 (Del. Ch. 2008) (denying motion to dismiss because "the complaint adequately pleads a claim of breach of fiduciary duty against a majority of the company's board of directors based on the alleged issuance and receipt of options not authorized by the company's plans."); *In re Tyson Foods, Inc.*, 919 A.2d 563, 593-94 (Del. Ch. 2007) (denying motion to dismiss where "Plaintiffs have alleged adequately that the Compensation Committee violated a fiduciary duty by acting disloyally and in bad faith with regard to the grant of options"); *cf. Provenz v. Miller*, 102 F.3d 1478, 1485 (9th Cir. 1996) (holding that directors' violations of their own internal policies shows falsity and scienter in fraud case). By departing from the Board's own executive compensation policy in approving and declining to rescind the 2010 executive compensation plan, the BioMed Directors breached their fiduciary duties of good faith and loyalty. Moreover, this is a Board that misrepresented to shareholders that the Company supposedly "pays for performance" while nevertheless granting lavish awards in the face of failure, and then maintaining its outrageous executive compensation plan despite shareholders' express rejection of that plan. Such a Board plainly was not "deal[ing] fairly and honestly with the shareholders for whom [it] is a fiduciary." *In re Tyson Foods*, 919 A.2d at 592.

Weiss, *Tyson* and *Ryan* are instructive. In all three cases, plaintiffs challenged stock option grants made by the directors pursuant to a shareholder-approved option plan. In denying defendants' motions to dismiss, the courts concluded that plaintiffs adequately pled claims of breach of fiduciary duty against the companies' boards based on the issuance of options not authorized by the companies' plans. *Weiss*, 948 A.2d at 437; *In re Tyson Foods*, 919 A.2d at 593-94; *Ryan*, 918 A.2d at 357-58.

In *Weiss*, the Court specifically noted that while compensation decisions are typically protected by the business judgment rule,

> the rule applies to the directors' grant of options pursuant to a shareholder-approved plan only when the terms of the plan at issue are adhered to. Thus, as the court held in *In re Tyson Foods, Inc. Consolidated Shareholder Litigation*, allegations in a complaint rebut the business judgment rule where they support an inference that the directors intended to violate the terms of shareholder-approved option plans.

Weiss, 948 A.2d at 441; *see also Ryan*, 918 A.2d at 357-58. The animating force behind these decisions calls for the same result here. Similar to *Weiss*, *Tyson* and *Ryan*, the Board has approved executive compensation that violated the terms of its executive compensation policy, thus further demonstrating the Directors' bad faith.

B. The Complaint Adequately Pleads A Violation Of Section 14(a)

1. The Legal Standard For Section 14(a) Claims

Proxy materials violate Section 14(a) and Rule 14a-9 where, as here: (a) they misrepresent a material fact or omit a material fact necessary in order to make the statement made not false or misleading; (b) the misrepresentation or omission was the result of knowing, reckless or negligent conduct; and (c) the proxy solicitation was an essential link in effecting corporate action. *See Mills v. Elec. Auto-Lite Co.*, 396 U.S. 375, 385 (1970). "Material information is information that, if disclosed in a proxy statement, would likely be viewed by a reasonable investor as having significantly altered the 'total mix' of information made available." *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976).

Contrary to Defendants' assertion (ID Br. at 19), Section 14(a) claims are subject to the liberal pleading standards of Fed. R. Civ. P. 8(a), not Rule 9(b). *See, e.g., Pension Comm. of Univ. of Montreal Pension Plan v. Banc of Am. Sec., LLC*, 446 F. Supp. 2d 163, 196 (S.D.N.Y. 2006) (Rule 8(a) applies "[w]here a plaintiff alleges a breach of fiduciary duty by conduct not

amounting to fraud, such as breach of a duty of care, disclosure, or loyalty, . . . not the heightened standards of Rule 9(b)"); *Gerstle v. Gamble-Skogmo, Inc.*, 478 F.2d 1281, 1300-01 n.20 (2d Cir. 1973) (plaintiffs seeking redress for a misleading proxy "are not required to establish any evil motive or even reckless disregard of the facts"); *In re Bank of Am. Corp. Sec., Deriv., & Employee Ret. Income Sec. Act (ERISA) Litig.*, 757 F. Supp. 2d 260, 321 (S.D.N.Y. 2010), *reconsid. denied*, 09 MD 2058-PKC, 2010 WL 4237304 (S.D.N.Y. Oct. 8, 2010) ("Liability can be imposed for negligently drafting a proxy statement."; rejecting defense argument that Rule 9(b) applied) (citing *Wilson v. Great Am. Indus., Inc.*, 855 F.2d 987, 995 (2d Cir. 1988); *In re Reliance Sec. Litig.*, 91 F. Supp. 2d 706, 729 (D. Del. 2000) ("negligence, not scienter, is the standard of liability under Rule 14a-9").[21]

A Complaint's use of terms such as "materially false" and "false and misleading" – terms which appear in Rule 14a-9, 17 C.F.R. §240.14a-9(a) – also does not subject Plaintiff's Section 14(a) to the Rule 9(b) pleading standard. *Bank of Am.*, 757 F. Supp. 2d at 321 (rejecting defendants' proposed application that "would treat any Rule 14a–9 claim quoting the underlying rule as one sounding in fraud").[22]

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[21] *See also, e.g.*, *In re Cendent Corp. Sec. Litig.*, 60 F. Supp. 2d 354, 378 (D.N.J. 1999) (because Section 14(a) claims require only that defendants acted negligently, a plaintiff "need not plead fraud at all, let alone fraud with particularity.").

[22] The Complaint here more than satisfies Fed. R. Civ. P. 8(a), and would even satisfy inapplicable heightened Rule 9(b) and PSLRA standards. Rule 9(b) only requires that the Complaint: "(1) specify the statements that the plaintiff contends were fraudulent, (2) identify the speaker, (3) state where and when the statements were made, and (4) explain why the statements were fraudulent." *Novak v. Kasaks*, 216 F.3d 300, 306 (2d Cir. 2000). Plaintiff meets these requirements: The Complaint here identifies and explains why the statements in the 2010 Proxy were false and misleading (*i.e.*, because executive compensation actually bore no meaningful relationship to performance), where and when the misstatements and omissions were made (in the Proxy, filed April 12, 2011), and who is liable for them (each Individual Defendant). *See also In re Scholastic Corp. Sec. Litig.*, 252 F.3d 63, 69-74 (2d Cir. 2001) (10(b) fraud case noting that

2. BioMed's Proxy Was Materially False And Misleading

Although Plaintiff's Complaint specifies Defendants' materially false and misleading statements and omissions in the Proxy, Defendants rest upon the demonstrably incorrect assertion that (supposedly) "Plaintiff has not identified a single false statement of material fact or material omission in the Proxy Statement." (ID Br. at 3; *see also id.* at 18-21 (quoting only one of the specific misstatements and omissions identified in Plaintiff's Complaint). In particular, the Complaint alleges that among the Defendants' materially false and misleading statements in the Proxy was that "the executive compensation awarded by the compensation committee is dependent *in large part* on the compensation committee's assessment of *corporate performance and the executives' individual and business unit performance*..." (¶¶ 30, 91) and that the Board's executive compensation program was designed "*to enhance BioMed's long-term financial performance and position, and thus stockholder value, by significantly aligning the financial interests of our executives with those of our stockholders*" (¶¶ 7, 29, 30, 91). The Proxy further stated falsely, *inter alia*, that the Board's executive compensation program was "designed" to "*promote individual accountability to deliver on t[the Company's] business objectives*" and achieve the "*aligning [of] our executive compensation structure with our stockholder's interests and market practices*." (¶¶ 7, 29-31, 91.)[23]

Contrary to its own stated executive compensation policy as presented to the shareholders

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"[e]ven with the heightened pleading standard under Rule 9(b) and the Securities Reform Act we do not require the pleading of detailed evidentiary matter in securities litigation"); *In re Initial Pub. Offering Sec. Litig.*, 241 F. Supp. 2d 281, 327 (2003) (Rule 9(b) can be satisfied in "one sentence").

[23] This information is plainly material. *See, e.g., Shaev v. Saper*, 320 F.3d 373 (3d Cir. 2003) (sustaining 14(a) claim and holding that information relating to executive compensation is material).

in the Proxy, and in violation of the Board's fiduciary duties, the Board unreasonably gave exorbitant executive compensation and granted large, undeserved pay hikes to the Company's top executives despite the Company's and Executive Defendants' *underperformance*. There can be no question that the material misrepresentations and omissions set out in the Complaint are false and misleading statements of fact, rather than merely (as Defendants wrongly assert) being "based on Plaintiff's subjective opinion that BioMed's 2010 executive compensation packages were not consistent with a 'pay-for-performance' philosophy" (ID Br. 20). This is no mere "disagree[ment] with the Board's evaluation of the executives' performance." (*Id.*) Rather, this is a matter of the Board saying one thing while doing something completely to the contrary. The sharp increases in executive compensation that the Board gave to the top executives (including the million dollar raise given to CEO and Board Chairman Gold, bringing is 2010 pay to over $5 million) completely fail to reflect the Company's poor performance. The Executive Defendants oversaw major declines in the Company's financials. Indeed, these executives eviscerated of earnings per share and the Company's net income, in addition to destroying stockholder value in posting a negative cumulative three year annual return for its shareholders when the Company's peers, and the RMS as a whole, were posting positive returns for shareholders in the same period. (¶¶ 5, 31, 37-39.)

Specifically, the Company's net income plunged from $60.19 million in 2009 to $39.31 million in 2010, a decrease of 34%. (¶ 37.) From 2009 to 2010, the Company's diluted earnings per share dropped from $0.45 in 2009 to $0.19 in 2010, a decline of more than 57%. (*Id.*) Furthermore, the cash dividend to common stockholders fell from $0.70 to $0.63. (*Id.*) In addition, BioMed's has substantially underperformed since 2007, posting Total Return "performances" well below the industry's leading indices, the S&P 500 and the RMS. (¶¶ 38-

39) (Company posted a *negative 3%* cumulative three-year annual total stockholder "return", trailing the *9%* cumulative three-year annual total stockholder return provided by the Company's peers and the *2.5*% cumulative three-year annual total stockholder return posted by the RMS).

Despite the executives' destruction of shareholder value and costing the Company (and shareholders) a fortune, and in complete disregard of the Board's stated policy to tie executive compensation to performance, the Board gave the Company's top executive massive pay hikes – giving the highest paid executive officers, defendants Gold, Griffin, and McDevitt collectively over $10 million in pay for 2010 – a *raise of 27.75%*, including a nearly $1 million boost for CEO and Chairman of the Board Gold, to give him a total of more than $5 million for 2010 (a 23.6% raise). (¶ 36.)

Accordingly, the Board's statements that its compensation was tied to performance, as detailed above and in Plaintiff's Complaint, were materially false and misleading. (¶ 91.) Further, the Defendants omitted from the Proxy material facts including particularly that executive pay was not tied to performance, while misrepresenting that the Board's executive compensation practices were firmly rooted in a pay-for-performance philosophy. (¶¶ 31, 91.)[24] At bottom, in choosing to speak, Defendants failed to speak the truth in violation of Section 14(a) and their fiduciary duties.[25] As articulated in *Tyson*, "[w]hen directors speak out about

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[24] Furthermore, the Board purported to "value the opinions of the stockholders" and will "consider the outcome of the vote when making future compensation decisions," but utterly failed to rescind or otherwise modify the excessive compensation it granted to the Company's top executive officers. (¶¶ 7, 92.)

[25] Contrary to Defendants' contentions (ID Br. at 21), the Complaint adequately pleads injury and satisfies the "essential link" element of a Section 14(a) claim. In addition to the harm of a misinformed shareholder vote on executive compensation, the Complaint alleges that the same misleading Proxy "also tainted the stockholder vote for the directors in addition to misleading shareholders regarding the Board's disloyal 2010 executive compensation scheme" (¶ 11), which

their own compensation, or that of company managers, shareholders have a right to the full, unvarnished truth." *In re Tyson Foods, Inc.*, 2007 WL 2351071, at n.18. *See also*, *e.g.*, *Shenker*, 983 A.2d at 338 ("[O]fficers and directors of a corporation stand in a sufficiently confidential relation to the corporation's stockholders to impose a duty upon them to reveal all facts material to corporate transactions.") (quoting *Parish v. Maryland & Virginia Milk Producers Ass'n*, 242 A.2d 512, 539 (1968)). The Individual Defendants thus breached their fiduciary duties and Section 14(a) through their material misrepresentations and omissions in the Proxy by which they solicited BioMed's shareholders to approve the 2010 executive compensation plan.

C. The Complaint States A Claim For Unjust Enrichment

As Defendants recognize, under Maryland law, "[a] claim for unjust enrichment is established when: (1) the plaintiff confers a benefit upon the defendants; (2) the defendant knows or appreciates the benefit; and (3) the defendants' acceptance or retention of the benefit under the circumstances is such that it would be inequitable to allow the defendant to retain the benefit without the paying of value in return." ID Br. at 22 (quoting *Benson v. State*, 887 A.2d 525, 546 (Md. 2005)). Defendants concede, as they must, that the first two elements of unjust enrichment are satisfied. *See id.* The third element has also plainly been met.

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is sufficient harm to state a claim for relief. *See, e.g., Weisberg v. Coastal States Gas Corp.*, 609 F.2d 650, 654 (2d Cir. 1979) (holding that "the challenged transaction is the election of the directors, and we have no doubt that the proxy solicitation itself . . . was an essential link in the accomplishment of that transaction") (internal quotation marks omitted). The fact that the say-on-pay vote went against the Board's recommendation has no impact on Plaintiff's Section 14(a) claim, as reliance is not an element of Section 14(a). *See Stahl v. Gibraltar Fin. Corp.*, 967 F.2d 335, 338 (9th Cir. 1992) (shareholder need not even vote to allege a Section 14(a) claim); *In re Countrywide Fin. Corp. Derivative Litig.*, 554 F. Supp. 2d 1044, 1075 (C.D. Cal. 2008) (sustaining 14(a) claim holding "interference with the processes of corporate democracy results in direct harm to the corporation [as well as] to shareholders who were actually deceived."); *cf. In re INFOUSA, Inc. Shareholders Litig.*, 953 A.2d 963, 990 (Del. Ch. 2007) (citing *Malone v. Brincat*, 722 A.2d 5, 14 (Del. 1998)).

Defendants base their erroneous position to the contrary on a gross mischaracterization of the Complaint, misstating that (supposedly) "Plaintiff alleges nothing more than the bare conclusion that it would be unjust to allow BioMed's executives to retain their 2010 compensation them [sic] given the Company's financial performance." *Id.* (citing nothing).

In particular, Plaintiff sufficiently pleads a claim for unjust enrichment against the Executive Defendants by alleging that, as a result of the Board's approval of the undeserved and unjustifiable 2010 executive compensation awards (and its bad faith failure to rescind those awards following the shareholder vote) in breach of the Board's fiduciary duties and stated pay-for-performance policy, these executives unjustly received (and continue to retain) excessive and undeserved compensation at the expense of the Company (which they must have known they were not entitled to and did not deserve). (¶¶ 84, 87-92.) Because it would be inequitable to allow the Executive Defendants to retain these funds given all of these factors (*i.e*., not just the Company's poor financial "performance" under their stewardship), Plaintiff has stated a claim for unjust enrichment.

Moreover, as the court explained in *Cox* in holding that the plaintiff stated a claim for unjust enrichment against the executives who received the allegedly improper compensation as a result of the Board's alleged breach of fiduciary duty, "Courts have repeatedly upheld claims of unjust enrichment despite defendants rendering services as employees, and 'the remedy of restitution may be invoked regardless of whether or not the party retaining the benefit is found to be a wrongdoer.'" *Cox*, 2011 WL 4383368, at *5 (quoting *Fleer Corp. v. Topps Chewing Gum, Inc.*, 539 A.2d 1060, 1063 (Del. 1988)). As here, the *Cox* "plaintiff allege[d] that defendants were unjustly enriched as a result of the Board's breach of fiduciary duty"; accordingly, "[a]t this stage of the pleadings, the Court conclude[d] that because plaintiff has sufficiently pled facts of

breach of fiduciary duty, it is 'axiomatic' that plaintiff has also sufficiently pled a claim for unjust enrichment." *Id.* (quoting *Jackson Nat'l Life Ins. Co.*, 741 A.2d at 394).

The facts set forth in the Complaint are easily sufficient at this stage to sustain Plaintiff's claim for unjust enrichment.

D. The BioMed Board Is Not Immunized By The Corporate Charter

Plaintiff has pled sufficient facts to demonstrate that the provisions of Biomed's corporate charter do not exculpate the Board from liability. As recognized by Defendants, under Maryland Law, a corporation's charter cannot immunize directors and officers from liability when the directors either (1) received an improper benefit, or (2) engaged in active and deliberate dishonesty. *See Hayes v. Crown Central Petroleum Corp.*, 78 Fed. Appx. 857, 865 (4th Cir. 2003) (citing Md. Code Ann., Courts & Judicial Proc. § 5-418); *see also Grill v. Hoblitzell,* 771 F. Supp. 709, 712 (D. Md. 1991). Plaintiff's Complaint alleges facts demonstrating both receipt of an improper benefit and that the directors engaged in active and deliberate dishonesty. As such, the Individual Defendants' motion to dismiss on this ground should be denied.

Plaintiff has alleged sufficient facts to demonstrate that Defendant Gold, BioMed's CEO and Chairman of the Board received an improper monetary benefit.[26] As a result of the Board's grant of excessive 2010 executive compensation, Gold received a total of $5.03 million in compensation for 2010, a 23.6% increase over his $4.07 million compensation for 2009, despite the fact that the Company's net income declined by over 34% from 2009 to 2010 and diluted

[26] Although Plaintiff has not alleged the receipt of improper benefit by the other directors, the fact that one director is receiving an improper benefit here can be sufficient to defeat the exculpation clause of the charter as to that director. *See*, *e.g.*, *Forgo v. Health Grades, Inc.*, C.A. No. 5716-VCS, at 27 (Del. Ch. Sept. 3, 2010) (Transcript Ruling) (finding that where the CEO/director had "powerful self-interest" and stood to receive "a benefit," a sufficient basis for defeating the exculpation clause existed). A copy of this transcript ruling is attached as Exhibit B to the Rosner Declaration.

earnings per share dropped from $0.45 in 2009 to $0.19 in 2010. (¶¶ 16, 37-39.) As alleged in Plaintiff's Complaint, this excessive compensation was improper given that the Company's executive compensation was supposedly designed to "achieve[]the desired goals of aligning our executive compensation structure with our stockholders' interests" and to reflect in large part "corporate performance." ¶¶ 30, 91. The notion that BioMed's CEO deserved a 23.6% increase in compensation for a year when the Company's financial performance had declined substantially is untenable. As alleged in Plaintiff's Complaint, BioMed's shareholders found this executive compensation plan to be grossly excessive and not in the best interests of the Company or its shareholders, voting down the Board's 2010 executive compensation plan. ¶¶ 43, 44. Thus, Plaintiff has alleged sufficient facts to demonstrate that Defendant Gold, a director who recommended and ultimately approved the Board's 2010 executive compensation plan, received an improper financial benefit as a result of his breach of fiduciary duty.

Plaintiff has further alleged sufficient facts to demonstrate that all members of the Board engaged in active and deliberate dishonesty in (falsely) representing that the Company's compensation policy was designed to reflect corporate performance and to align with stockholders' interests. Although Maryland courts have not interpreted what constitutes "active and deliberate dishonesty" under Md. Code Ann., Courts & Judicial Proc. § 5-418(a)(2), in *Felker v. Anderson*, No. 04-CV-W-IDS, 2005 WL 602974, at *4 (W.D. Mo. Feb. 11, 2005), the court interpreted Maryland law and found that active and deliberate dishonesty existed where plaintiff alleged that defendants were involved in "producing, reviewing, disseminating, approving, ratifying and/or reckless permitting the dissemination of false and misleading statements and information."

Plaintiff has plainly alleged that the Board was actively engaged producing, reviewing, approving and ratifying false and misleading statements to shareholders regarding the 2010 executive compensation structure. In the Proxy, Defendants falsely claimed, *inter alia*, that the Board's executive compensation policy was firmly rooted in a pay-for-performance policy, including being designed to "enhance BioMed's long-term financial performance and position by significantly aligning the financial interests of our executives with those of our stockholders." (¶¶ 7, 29.) Defendants claimed that the 2010 executive compensation policy was based in "large part" on "corporate performance," yet the Board recommended and approved the 2010 executive compensation structure which significantly increased executive compensation for the year despite a substantial decline in net income and earnings per share. (¶¶ 37, 91.) The Board chose to increase executive compensation by more than 27% when the Company lost a bundle of money and posted a negative 3% cumulative three-year annual total stockholder return, trailing the 9% cumulative three-year annual total stockholder return provided by the Company's peers. (¶¶ 29-31, 38-39.) Defendants stated that they "value the opinions of stockholders" and will "consider the outcome of the vote when making future compensation decisions," but have remained inexplicably silent regarding the say-on-pay vote rejecting the 2010 executive compensation and have taken no action in response to the shareholder vote. (¶ 9.)

Based on these allegations, it is clear that Plaintiff has set forth sufficient facts to demonstrate that the Board engaged in deliberate and active dishonesty in making false and misleading misrepresentations to shareholders. Indeed, Defendants must have known that the Proxy was materially false and misleading when made, given that their high-level positions and access to BioMed's internal information obviously would have revealed to them that granting the excessive 2010 executive compensation while BioMed's financial performance declined violated

the Board's stated pay-for-performance executive compensation policy as outlined in the Proxy disseminated to shareholders. (¶ 52.)

As such, BioMed's corporate charter cannot insulate the Board from liability.

E. Pre-Suit Demand Would Have Been Futile Because The Directors Were Committed To Their Decision To Maintain The Excessive 2010 Pay Packages

The purpose of a derivative action is to "place in the hands of the individual shareholder a means to protect the interests of the corporation from the misfeasance and malfeasance of 'faithless directors and managers.'" *Shenker v. Laureate Educ., Inc.*, 411 Md. 317, 342, 983 A.2d 408, 420 (Md. 2009) (citing *Danielewicz v. Arnold*, 137 Md. App. 601, 769 A.2d 274 (2001)); accord *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 95-96 (1991). Rule 23.1 establishes a pleading standard for derivative actions in federal court, and is satisfied where, as here, a derivative plaintiff pleads that he has made a pre-suit demand on the board of directors to commence the action or plead with particularity the reasons why such efforts were not made. *See* Fed. R. Civ. P. 23.1(b)(3); *Halebian v. Berv*, 590 F.3d 195, 211 (2d Cir. 2009). Because nominal defendant Biomed is a Maryland corporation, demand futility is governed by Maryland law. *Kamen*, 500 U.S. at 108-109. Under Maryland law, as explained by the Court of Appeals of Maryland in its seminal decision in *Werbowsky v. Collomb*, demand on the board of directors of the nominal defendant is excused when a plaintiff alleges that:

> a majority of the directors are so personally and directly conflicted or committed to the decision in dispute that they cannot reasonably be expected to respond to a demand in good faith and within the ambit of the business judgment rule.

362 Md. 581, 620, 766 A.2d 123, 144 (2001). Plaintiff has more than satisfied the Rule 23.1 pleading standard because it is indisputable that a majority of the Directors (indeed, the entire Board) are plainly directly "committed to the decision" to maintain the challenged compensation packages (as well as certain of the Directors being obviously conflicted).

First, Biomed concedes that two members of the Company's seven member Board, defendants Gold and Kreitzer, are Biomed executives and are not independent, and Biomed does not (and cannot) argue that demand would have been futile as them. *See* ND Br. at 3, 13. Moreover, Biomed cannot seriously argue that Gold is not "personally or directly conflicted" and thus would have been able to respond in good faith to a demand. Gold is one of the executives alleged to have received an outsized raise and failed to decline the excessive pay after it was rejected by the Company's shareholders. Indeed, Gold's pay was raised by nearly $1 million (a year-over-year increase of more than 23%, to bring his total package to over $5 million), more than any other executive subject to this litigation.

Second, demand would have been futile as to each of the director defendants. In moving to dismiss, Biomed completely ignores the controlling language of the Court of Appeals decision in *Werbowsky*, which holds that a director could not have properly considered pre-suit demand where he is so "committed to the decision" under attack that he be "cannot reasonably be expected to respond to a demand in good faith and within the ambit of the business judgment rule." *Werbowsky*, 362 Md. at 620, 766 A.2d 123, 144. The Board's conduct – in maintaining the 2010 pay hikes in disregard of the shareholders' public demand through their vote that the Board rescind them – plainly demonstrates that the Directors were so committed that they thus could not have been expected to fairly consider a demand from Plaintiff.

Further, three of the director defendants, Cambon, Dennis and Gilchrest served on the Compensation Committee and thus were directly responsible for devising the compensation awards challenged in this case (and who, together with Gold and Kreitzer, constitute a majority

of the Board, *i.e.*, 5 of 7 directors).[27] Each of the director defendants approved the compensation awards challenged in this lawsuit, and recommended their approval to Biomed's shareholders in the Proxy (by way of allegedly material misrepresentations). Each of the director defendants also decided not to rescind the compensation awards after Biomed's shareholders repudiated the Board's compensation proposal and by majority vote disapproved those packages.

It is simply inconceivable that, after having devised, approved, promoted and then failed to rescind the pay packages after the majority of Biomed's shareholders voted against the them (collectively voicing their demand that the compensation awards be rescinded or otherwise modified downward) that the Board would have seriously considered reversing course and suing itself and others for this misconduct because of a single shareholder's demand. The United States District Court for the Southern District of Ohio recognized this truism in *Cox*, the similar "say on pay" discussed above, explaining:

> [T]he directors did not merely approve the transaction, they also recommended to the shareholders that the shareholders approve the compensation. Given that the director defendants devised the challenged compensation, approved the compensation, recommended shareholder approval of the compensation, and suffered a negative shareholder vote on the compensation, plaintiff has demonstrated sufficient facts to show that there is reason to doubt these same directors could exercise their independent business judgment over whether to bring suit against themselves for breach of fiduciary duty in awarding the challenged compensation.

[27] *Werbowsky* only requires that a demand futility be established as to a majority of the Board. Thus, even if the Court determines that demand would not be futile as to Kreitzer and the two non-employee directors who did not serve on the Compensation Committee, demand would still have been futile because Gold and the three Compensation Committee directors were obviously most committed to the decision to press on with the rejected compensation awards, and those four directors constitute a majority of this seven-member board.

2011 WL 4383368, *4 (denying motion to dismiss under Ohio law where defendants argued that plaintiff had failed to plead why pre-suit demand would be futile).[28]

Werbowsky and its progeny cannot be read to require pre-suit demand on a board so demonstrably committed to its decision, as the BioMed Board is here.[29] The *Werbowsky* Court noted that making pre-suit demand is often preferable because it gives directors:

> an opportunity to consider, or reconsider, the issue in dispute. It may be their first knowledge that a decision or transaction they made or approved is being questioned, and they may choose to seek the advice of a special litigation committee of independent directors, which has become a common practice, or they may decide, as a business matter, to accede to the demand rather than risk embarrassing litigation.

Werbowsky, 766 A.2d at 144. These considerations would not be served by requiring demand under these circumstances. The director defendants have considered the compensation awards at issue (through the Compensation Committee's determination), reconsidered the awards (though the determination of the full board, as well as the full board's decision to recommend approval to shareholders), and were given the opportunity to reconsider the packages *again* after suffering

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[28] Defendants note that *Cox* was decided under Ohio law, which diverges from Maryland law. Plaintiff cites *Cox* for the Court's recognition that there is reason to doubt that directors acting under similar circumstances could be expected to properly respond to a shareholder demand. Nor should the Court be swayed by Biomed's reliance on two non-Delaware cases decided under Delaware, *Teamsters Local 237 Additional Security Benefit Fund v. McCarthy*, No. 2011-CV-197841 (Ga. Super. Fulton County Sept. 16, 2011) and *In re Jacobs Engineering Group, Inc. Consol. S'holder Deriv. Litig.*, No. BC457808 (Cal. Super. Ct. Los Angeles County Nov. 10, 2011). Delaware's approach to demand futility was expressly rejected by Maryland in *Werbowsky*. 766 A.2d at 143. Notably, the Delaware test, which was described by the *Werbowsky* court as exacting, does not include any concept analogous to Maryland's "committed to the decision" standard. *See generally id*. Accordingly, Defendants' reliance on *McCarthy* and *Jacobs* is unavailing.

[29] Notably, Defendants do not cite any decision dismissing a derivative action under Maryland law for failure to demonstrate that demand would have been futile where either a board was given as many chances as Biomed's board had to reconsider its decision, or where, as here, a board remained committed to its decision in direct contravention of a shareholder vote.

the negative shareholder vote. Maryland law does not require that a board be given chances to consider their conduct *ad infinitum* before demand is excused. *See id*. at 143 (declining to eliminate the demand futility exception). Nor is it likely that the director defendants would have fairly considered a demand to avoid the embarrassment of shareholder litigation; such litigation is surely less embarrassing than being one of the miniscule number of boards that has been publicly rebuffed by shareholders in a "say on pay" vote. *See Cox*, 2011 WL 4383368, n.2 (noting study finding that "only 1.6% of public companies which have held their annual meetings as of the end of June 2011 received negative shareholder recommendations"); ¶ 4 ("Of the approximately 2,500 companies that have held say-on-pay votes since the enactment of the Dodd-Frank Act, only 38, or 1.5%, have failed to receive shareholder support for their executive compensation.").

Accordingly, Plaintiff has easily met his pleading standard under Rule 23.1 and Biomed's motion to dismiss should be denied.

VI. CONCLUSION

The Individual Defendants' Motion to Dismiss and the Nominal Defendant's Motion to Dismiss should both be denied in their entirety.

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